THE COMPANIES ACT 1993: PITFALLS AND PROSPECTS FOR REFORM*

Introduction

I have been asked to speak today about some significant pitfalls that corporate advisers need to be aware of, when giving advice about companies incorporated under the Companies Act 1993. My focus is on the role of directors, and their relationship with shareholders. More specifically still, my focus is on how the directors of a company can ensure that transactions are validly authorised, in a manner which ensures that the company is entitled to enter into the transaction, and minimises the risk of claims against the directors by existing shareholders, or new shareholders, or a liquidator where the company subsequently becomes insolvent.

Directors take business decisions that involve risks: that is their job. Minimising the prospect of claims concerning business decisions that were taken in good faith, but that turned out badly, brought with the benefit of hindsight and involving considerable cost and risk, some years down the track, is often, understandably, an important issue for directors.

These issues tend to be most acute for small and medium sized companies, as they are less formally run, and are more likely to enter into transactions with shareholders and related parties that are influenced by personal or other non-commercial factors. It is that mix of informality and personal factors that tends to give rise both to difficult questions under the 1993 Act, and to the risk of subsequent disputes.

In the time available, I propose to focus on three issues:

- shareholder decision making, and shareholder approval/ratification of board decisions. How much comfort do these give directors? What are the implications for shareholders?

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- delegation by directors;

- some of the more problematic aspects of directors' duties under the 1993 Act.

I will begin by outlining briefly some of the relevant provisions, and identifying some of the issues that directors and their advisers can encounter. I then suggest some possible reforms, which would in my view lead to a more appropriate balance between facilitating commercial activity and the taking of business risks, and accountability to shareholders and creditors.

It is helpful to have a concrete example in the back of our minds as we discuss these issues. Let us take, as our illustration today, a closely held company called Paradise Puddings Limited ("PPL") which has been set up to produce gourmet desserts for sale through retail outlets, and for home delivery, in the Auckland area. PPL has three shareholders: a couple, Sam and Lynn, who run the business on a day to day basis, each of whom holds 1,000 shares; Paul, an Auckland barrister who in a rash moment over a passionfruit pannacotta and a few glasses of dessert wine agreed to provide most of the capital for the business (who holds 5,000 shares) and Sarah, a graphic designer who was issued 500 shares in exchange for designing PPL's logo, packaging etc.

The directors of PPL are Sam and Lynn, but they regularly catch up with Paul (over dessert and a glass of wine, of course) to discuss the company's business with him. Sarah has moved to Sydney, and is not included in these discussions.

The power to manage the company

The default rule under the 1993 Act is that the board is responsible for the management of the company. The power of management is conferred by the Act, rather than being delegated by shareholders. Section 128 provides that the business and affairs of the company must be managed by, or under the direction or supervision of, the board of the company. The board has all the powers necessary for managing, and for directing and supervising the management of, the business and the affairs of the company.

The company's constitution can provide for "modifications, exceptions or limitations" in respect of conferral of powers. The constitution of PPL, for example, could provide that certain decisions of the board (such as entering into a long term lease) require Paul's approval, or approval by the shareholders by ordinary resolution.

The constitution of the company can also provide that certain decisions that would otherwise fall to be made by the board, under section 128(1) and (2) must instead be made by some other person, or by the shareholders. The better view is that this is possible in respect of management powers, though probably not some other director powers: it can be seen as a "modification" for the purposes of section 128(3). This is discussed in more detail below.

The provisions of the Companies Act imposing duties on directors, and some related provisions discussed in this paper, are set out for ease of reference in the appendix to this paper. Of particular importance for today's purposes are:

- section 131, imposing a duty on directors to act in good faith and in what they believe to be the best interests of the company;
- section 133, requiring directors to exercise a power for a proper purpose;
- section 135, imposing liability on directors who agree to the business of the company being carried on in a manner likely to create a substantial risk of serious loss to the company's creditors, or who cause or allow this;
- section 136, which provides that a director must not agree to the company incurring an obligation unless the director believes at that time on reasonable grounds that the company will be able to perform the obligation when it is required to do so;
- section 137, which sets out the statutory duty of care of directors;
- sections 139-141, which concern transactions in which a director has an interest.

Shareholder involvement in company management

There are a number of ways in which shareholders who are not directors of a company may become involved in the making of a management decision. Possibilities include:

- informal participation in director decision making, including through consultation on a particular issue, or generally;
- approval of decisions for which the Act requires shareholder approval (eg major transactions, which require shareholder approval under section 129);
- approval of matters in respect of which the Act expressly contemplates the possibility of shareholder decision-making in place of the directors. Section 107 provides for certain matters to be decided by shareholders rather than directors;
- shareholder approval/ratification of director decisions, where this is required by the company's constitution (but not by the Act itself);
- shareholder exercise of a particular decision making power, where the company's constitution provides that the matter in question is to be decided by shareholders rather than by directors;
- ad hoc approval/ratification by shareholders of a particular decision made by directors. This may be formal, expressed in a written resolution, or informal, through acquiescence in the decision;
- ad hoc decision making by shareholders, who authorise the company to enter into a particular transaction on a one off basis, though this is not provided for in the Act or in the company's constitution;
- ratification of breaches of duty by directors, after the event.

The implications of each of these forms of shareholder participation in a management decision are explored in more detail below.

Informal participation in company management

Paul, as mentioned above, is often consulted by Sam and Lynn about business decisions. Is this enough for him to be a deemed director? There is a real possibility of a finding to this effect, in reliance on either s126(1)(a) ("persons occupying the position of director of the company, by whatever name called") or s126(1)(b)(ii) ("a person in accordance with whose directions or instructions the board … is accustomed to act").[1]

The outcome will very much depend on the extent of Paul's involvement in the management of the company – and whether, for example, the informal chats with him are in fact the decision making process for the management of the company, or whether they simply inform some of the decisions made by the directors. This highlights one important pitfall for shareholders: the greater their involvement in the day to day affairs of the company, the more actively they seek to protect their interests through consultation with the directors, and the more frequently the directors accede to their wishes, the greater the risk that they too will ultimately be held to be directors for certain purposes. Shareholders like Paul, who have chosen not to be appointed as directors, need to be aware that a decision to take an active interest in the company and to influence day to day management decisions creates the very real risk of becoming a deemed director.

Note that, whatever Paul's status, Sam and Lynn are clearly still responsible for the decisions they make: Paul's informal participation in decision-making does not affect their duties. The practical risk of Paul disagreeing with decisions is reduced, and Paul would face some difficulties in challenging a decision he had agreed with (on the basis of full information). But these informal discussions would not preclude claims by Paul, let alone by any other shareholder, or by a liquidator in the event of insolvency.[2]

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[1] For a discussion of s126(1), see *Fatupaito v Bates* (2001) 9 NZCLC 262, 583.

[2] Note also that because one (minor) shareholder is not involved in these discussions the time for setting aside a transaction in which a director is interested, under s141, will not start running until Sarah has also received adequate disclosure.

Shareholder approval required by Companies Act

Suppose that Sam and Lynn wish to enter into a lease of new premises for PPL, and that the transaction amounts to a major transaction for the purposes of section 129. (I put to one side the difficulty of determining, in such cases, whether the lease is indeed a major transaction.) The transaction must be approved by a special resolution, or contingent on approval by special resolution. Suppose all the shareholders except Lynn (who is reluctant to agree to this commitment) sign a written resolution authorising entry into the transaction. What obligations do the shareholders have in making such a decision? What risks, if any, are they taking? Are the directors absolved of responsibility for the transaction?

The question is whether the major transaction procedure is better seen as the directors deciding to enter into a transaction and receiving shareholder approval to do so, or whether the shareholder approval is a substitute for director approval. A secondary question is whether, if the former is the better analysis, that shareholder approval has any impact on the responsibility of the directors for their decision.

It seems reasonably clear that shareholders voting on a major transaction for section 129 purposes are not deemed to be directors for that purpose: none of the limbs of section 126 applies. So shareholders are able to vote in their own interests, rather than being required to act in the interests of the company. And they will not incur any liability to creditors even if there is a breach of s135 or s136. The shareholders are required to approve such transactions to protect their own interests, and the broader responsibilities provided for under the Act remain with the directors. This is entirely consistent with the policy rationale underpinning s129: if certain fundamental changes are proposed in respect of the business of the company, a 75% majority should be free to decide how they wish their assets to be employed, and not frustrated in pursuing their commercial objectives by the minority. But the minority is not required to live with the majority's preferred outcome: they are entitled to exit at a fair price.[3] The minority buy-out regime (including provision for voting in separate interest

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[3] See *Morison's Company and Securities Law* paras 16.9, 16.15 ff.

groups) and the major transaction regime assume that shareholders are voting in what they perceive to be their own separate commercial interests. The absence of any “deemed director” duties is consistent with this.

This suggests that the implicit model for major transaction decision making is that it is still the decision of the directors whether or not to enter into the transaction, and they are subject to all the normal duties in connection with that decision, but in addition require shareholder approval. If the directors decide to enter into the lease, and the s129 shareholder approval is obtained, the transaction is validly authorised for internal company purposes.

Does a section 129 approval excuse directors from any of their duties? Under the pre-1993 law, a transaction that was voidable at the instance of a company due to a breach of directors’ duties could be ratified by an ordinary resolution of shareholders, with full disclosure of the relevant breach, and this would cure the defect. Shareholder ratification of the board decision also precluded any claim by the company against the directors, provided disclosure was adequate and no question of insolvency arose.[4] Cases such as *Re Duomatic Ltd* [1969] 2 Ch 365, [1969] 1 All ER 161 went further still, and established that informal shareholder approval, or acquiescence in a course of action, could suffice to validate a corporate act.

Under the 1993 Act it is not easy to see why shareholder approval should excuse directors from their s135 and s136 duties. And there is no obvious basis for distinguishing between those provisions and the other duty provisions. The

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[4] Such ratification would also be ineffective in certain cases where the ratification was procured by interested directors voting to ratify their own wrongdoing for the pre-1993 law on shareholder approval/ratification of board decisions. See generally *Bamford v Bamford* [1969] 1 All ER 969 (CA); *North-West Transportation Co Ltd v Beatly* (1877) 12 App Cas 589 (PC); *Millers (Invercargill) Ltd & Ors v Maddans* [1938] NZLR 490 (CA); *Westpac Securities Ltd v Kensington* [1994] 2 NZLR 555 (CA); *Pascoe Ltd v DFC Overseas Investment Ltd* [1994] 3 NZLR 627; Halsbury vol 7(1) paras 620, 626, 955, 970. In the context of an application for leave to bring a derivative action against directors in respect of (inter alia) allegedly excessive salaries, which had also been approved by shareholders in general meeting (the directors being the majority shareholders), Master Venning (as he then was) treated the common law on ratification as applicable under the 1993 Act, and saw the issue as turning on the exceptions to that rule. But there does not appear to have been any argument about the application of the common law authorities under he 1993 Act, so the decision is of limited weight on this point. See *McFarlane v Barlow* (1997) 8 NZCLC 261,470.

absence of shareholder liability in respect of a s129 vote is also a pointer to continuing director liability. So the better view is that shareholder approval under s129 does not affect the legal responsibility of directors for the transaction in question. At most, shareholder approval (at a time when no solvency issues are present) may have some presumptive or evidential value on the questions whether the transaction is in the best interests of the company, has been entered into for a proper purpose, and involves no breach of the directors' duty of care. [5]

This highlights one of the first pitfalls for directors that I want to emphasise today: shareholder approval of a transaction under section 129 probably does not relieve directors of any of their responsibilities to the company, and in particular does not affect their exposure under sections 135 and 136, if the company runs into financial difficulties.

Notice also that unless the shareholder approval is unanimous and is given under s107 (discussed below), it does not affect the operation of the 'interested director' provisions. The interest must still be entered in the interests register (s140(1)), and the transaction is still liable to be set aside under s141. This significantly limits the use of shareholder approval as a mechanism to decide on transactions in which a director has an interest. However a notice of a meeting to consider the transaction that is sent to all shareholders, or other disclosure to all shareholders in connection with seeking their approval, will start time running for the purposes of s141. (Note that a s122 resolution signed by some shareholders only will not achieve this.) And the greater the degree of notice to shareholders, and shareholder approval, the less the risk of a successful attempt to challenge the transaction, or to seek other relief against the director in question.

Unanimous shareholder decisions under section 107

Section 107 makes express provision for unanimous shareholder approval of certain corporate acts, and disapplies the provisions that would otherwise govern

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5 For a more optimistic assessment of whether common law rules concerning shareholder ratification and unanimous shareholder approval have survived under the 1993 Act see *Morison's Company and Securities Law* paras 25.42-25.44; Peter Watts, "Unanimous Shareholder Assent and the Companies Act 1993" [1994] CSLB 26.

those acts. In respect of share issues, for example, a unanimous shareholder approval means none of the board resolutions and certificates contemplated by sections 42, 44 and 45-49 is required.[6]

However section 107 does not apply to management decisions generally, and in particular it does not apply to a decision to enter into a particular transaction. Section 107 is further limited by the requirement of written agreement, the special rules on notice following action taken in reliance on a general and continuing agreement, and the (commercially bizarre) provision for withdrawal from such agreements.

Where section 107 does apply, the better view appears to be that directors are relieved of the responsibilities imposed by the provisions that are expressly disapplied. But they retain their general duties, so far as relevant, under sections 131-140. In addition, they have a solvency certificate obligation under section 108 in certain cases.

Approval by shareholders pursuant to constitution

What if the constitution of PPL provides for board decisions on certain matters, say transactions involving expenditure of more than $100,000, to be approved or ratified by shareholders? In these circumstances, the position appears to be that:

- the directors are required to make a decision to enter into the transaction. So they have all their usual duties, and are exposed to the usual liabilities;

- the shareholders who take part in making the decision are also treated as directors for the purposes of section 131 to 138: see section 126(3).

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6 It was suggested by Potter J in *Re Gellert Developments Ltd* (2002) 9 NZCLC 262,942 that shareholders approving director remuneration under s107(1)(f) were required to apply the s161 test of whether the remuneration was fair to the company (para 63). With respect, this cannot be correct: s107(1)(f) itself speaks of authorisation “otherwise than in accordance with [s161]”. The Judge found that the salaries credited pursuant to the shareholders’ resolution were excessive (para 43), and held that this amounted to a breach by the directors of their duties (para 67(b)). How a resolution of the shareholders could amount to a breach of directors’ duties is nowhere explained. Nor did these findings play any part in the relief granted, which was granted against the sole director at the relevant time and not against the other (non-director) shareholder, and was quantified by reference to another breach of duty. Overall, it is suggested this decision provides no assistance on the interplay between s107 and the duties of directors.

The second point bears some elaboration. When approving management decisions by virtue of a provision in the company's constitution, shareholders have the full range of director duties. They cannot simply vote in their own interests: they must act in good faith and in what they believe to be the best interests of the company; they must act for a proper purpose; they must exercise the care and skill of a reasonable director, and so forth. Some of these duties are not readily applied to shareholders. And simply by virtue of taking part in the decision they are subject to the duties imposed by ss135 and 136: though presumably if they vote against the transaction, they have not agreed to it, so are not liable.

It is far from obvious why the position of shareholders should be different from that which applies in the major transaction context, under section 129. If directors are approving entry into the transaction, and assuming the statutory responsibility for that transaction, it is more sensible for shareholders to be seen as acting to protect their own interests, rather than as substitute decision makers in place of the directors. It seems to me that that is how shareholders are likely to understand a reference to them for their approval, and that this is a reasonable common-sense understanding. In particular, shareholders who are not involved in the day to day management of the company certainly are not well-placed to make the solvency judgements contemplated by sections 135-136. And they cannot generally be expected to exercise the skill and care of a reasonable director: they have not taken on that role, and do not usually have access to the necessary information to meet this standard. Thus the shareholder decision on approval should not be subject to the various 'other-regarding' obligations (eg to act in good faith and in the best interests of the company) provided for in the Act, and should not attract liability consequences under sections 135 and 136.

The provision imposing duties on shareholders in this context may have been inspired by the caselaw on the limits on the ability of a majority shareholder to vote to approve or ratify his or her own wrongdoing as a director. But it is a particularly inept instrument to address this concern, as:

- it is unnecessary, if (as I have suggested above) ratification of transactions by shareholders is ineffective to excuse directors from liability in respect of

interested transactions under the 1993 Act, except where unanimous approval is obtained under s107;

- it goes too far, in imposing director responsibilities on all shareholders in all circumstances: it is a very blunt, very large instrument to address a very specific concern.

As mentioned above, shareholder approval of a transaction in which a director is interested does not disapply the ‘interested director’ provisions, unless unanimous approval is given under s107. Where a company constitution requires certain transactions in which a director or majority shareholder is interested to be approved by shareholders, or by independent shareholders:

- that provision is effective as a limit on the authority of the directors, at least as a matter of internal corporate governance;

- but the fact that such approval has been obtained does not, in my view, affect the duties of the directors or the application of ss140-141.

Shareholders are often unaware of the nature and extent of their duties when voting on whether or not to approve transactions, pursuant to the company’s constitution. If they were so aware, their enthusiasm for voting would almost certainly be affected, in ways that undermine any real attempt at shareholder participation.

The current rule imposing director duties on shareholders seems unnecessary and in many respects counterproductive. Creditors are no worse off if directors seek shareholder approval confined to shareholders’ own interests, provided directors retain their responsibilities to creditors. Directors should be able to put significant matters to shareholders and act in reliance on their decision, so far as the interests of shareholders are concerned (and for a solvent company, the interest of shareholders should be decisive – it is after all their money). And shareholders should be able to stipulate ex ante, in the company’s constitution, that certain steps must not be taken unless they agree – without thereby falling under duties to the company concerning how they vote, and concerning the position of creditors. There is no apparent policy justification for the different approaches to

shareholder approvals required under section 129, and approvals required by a company's constitution.

Directors for their part, need to be conscious that shareholder approval or ratification gives them no legal protection under the 1993 Act. However, as discussed above, shareholder approval, even if legally ineffective to exclude certain duties, does in my view provide some evidence that certain duties have been discharged, and in particular that a particular transaction is in the best interests of a company, and that it has been entered into for a proper purpose, at least where the company's solvency is not in doubt.

Shareholder decision making in accordance with the constitution

Rather than merely requiring shareholder approval of a decision by the board to enter into a particular type of transaction, the constitution of the company may provide for shareholders to make certain decisions themselves, in specified circumstances. Suppose, for example, that the constitution of PPL provides that any decision to enter into a lease for a term of more than 12 months must be made by shareholders, and not by directors.

It appears that such a provision is effective: it is a "modification" for the purposes of section 128(3), and the ability of the constitution to reallocate powers in this way is assumed by sections 126(1)(b)(iii) and 126(2). So if PPL proposes to enter into a five year lease of new premises, the directors are not able to approve entry into that transaction. Rather, the shareholders must make this decision. In making that decision the shareholders are deemed to be directors for the purposes of sections 131 to 138 (s126(2))[7]. This means that:

- the shareholders are required to act in good faith and in what they believe to be the best interests of the company. They cannot vote in their own separate

[7] It might also perhaps be argued that in such circumstances, the shareholders fall within section 126(1)(a), and are persons "occupying the position of director of the company by whatever named called". But in my view this unduly strains the language of that limb of section 126, which is directed at people who are in practice managing the affairs of the company generally, though not appointed as directors.

commercial interests. This is a significant issue, of which shareholders are likely to be unaware;

- shareholders who take part in making the decision and vote in favour of entry into the lease are exposed to claims for breach of sections 135 and 136. Suppose for example that the company is only marginally solvent, and there are no reasonable grounds for believing that the company will be able to pay the rent throughout the term of the lease.[8] The shareholders risk personal exposure to the lessor, via section 136 and a claim by the liquidator in the name of the company. The protection of limited liability is substantially reduced, in these circumstances.

The directors, on the other hand, appear not to have any corresponding responsibility for these transactions. They are not deciding to approve them: their function is the purely ministerial one of giving effect to the decision of the shareholders. They cannot even be said to be agreeing to the company incurring the obligation, or agreeing to the business being carried on in a manner likely to create a substantial risk of serious loss to creditors, in circumstances where they have no authority whatsoever in respect of the matter in question. (However, they may of course face some exposure in respect of subsequent trading, and other obligations entered into after the lease has been taken on.)

There are some curious differences, in this context, between the position of shareholders on whom a power to make these decisions is conferred, and the position of other persons on whom such powers are conferred. In particular, the section 301 procedure for bringing claims against a director is available against a person who is entitled to exercise a power which, apart from the constitution of the company would fall to be exercised by the board, but that procedure does not appear to be available against shareholders by virtue of section 126(2). There is no obvious reason for this distinction.

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[8] Compare *Ocean Properties Ltd v Everest & Heys* (2000) 8 NZCLC 262,289, where a lessor obtained orders against a director under s301 in respect of unpaid rent, where the company entered into the lease of a time when it had no assets and no immediate prospect of business income to fund the rent.

The difference between the Act’s treatment of shareholder approval/ratification and shareholder decision-making is to some extent justified, so far as duties reflecting the interests of third parties are concerned. Plainly the responsibility to ensure solvency issues are taken into account cannot be left floating in the ether, with neither directors nor shareholders being accountable. But it still seems unrealistic to say that shareholders have the duties set out in sections 135 and 136, if they do not have the level of familiarity with the financial position of the company, and access to information and advice, which those provisions contemplate. And the current rule strongly discourages shareholder participation in such votes. A better approach would be to make it clear that directors cannot rely on shareholder approval if they know the company is, or may be, insolvent: that is, the directors are still required to address the solvency issue, not the shareholders, and if they get it wrong then they are not protected by the shareholder decision.

Ad hoc approval/ratification of board decisions by shareholders

Suppose that PPL proposes to enter into a transaction that it is within the power of the board to approve. Neither the Act nor PPL’s constitution requires the decision to be made or approved by shareholders. Suppose however that directors are anxious to minimise their exposure to claims in respect of the transaction, and seek shareholder approval. If the shareholders approve entry into the transaction by written resolution, what is the legal effect of that approval?

As the law stood before the 1993 Act, an ad hoc resolution of shareholders approving or ratifying entry into a transaction gave directors and persons dealing with the company considerable comfort that the transaction was properly authorised, and that the company could not subsequently seek to set aside the transaction. Unanimous shareholder approval, and probably even approval by general resolution in most cases, precluded claims by the company for breach of

director duties, provided full disclosure of relevant interests and breaches was made to the shareholders.[9]

Under the 1993 Act, however, it is far from clear that such resolutions have any legal effect. The High Court has assumed on at least one occasion that the *Duomatic* principle has survived under the 1993 Act.[10] But it is not easy to see why this is so. The directors are not bound to act in accordance with any shareholder resolution on management matters, as section 109 makes clear. So the decision to enter into the transaction remains the decision of the directors. None of the directors' duties are transferred to the shareholders under section 126, as is the case where the constitution provides for shareholder approval or shareholder decision making.

If the company were subsequently to bring proceedings against the directors, for example for breach of their duty of care, the best argument available to the directors would probably be that the resolution amounted to a ratification by shareholders of their decision. However ratification by a body corporate must be approved by the organ of that body corporate that has authority to make the decision in question: since shareholders do not have the authority to enter into the original transaction, or to make the decision whether or not to take proceedings against the directors or settle such proceedings, in terms of the scheme of the Act and the basic allocations of powers it contemplates, it is difficult to see what effect a purported ratification would have. Nor is it easy to see why ratification by shareholders should affect the application of ss135 and 136. In circumstances where the shareholders do not become deemed directors, and do not have any responsibilities to creditors, it seems to me that a Court will almost inevitably hold that sections 135 and 136 continue to apply to the directors. The duty to act in

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9 However such approval would not affect liability of directors under insolvent trading or reckless trading regimes, and might be ineffective if the company was insolvent, or if interested directors voted to ratify their own wrongdoing, or if the decision involved expropriation of the company in favour of shareholders voting in its favour. The legal basis for the shareholder approval rule was less than clear, given the basic principle that shareholders could not usurp functions conferred on directors under the Articles, but the rule was well established in both England and New Zealand.

10 See *Kitchener Nominees Ltd v James Products Ltd* (2002) 9 NZCLC 262,882 at para 32(b).

good faith and in the best interests of the company under section 131 is also unlikely to be affected.

It cannot be stressed too strongly that the conceptual underpinning for giving effect to such resolutions that applied under the previous legislation simply is not available under the 1993 Act. Directors are not agents who derive their powers from members by virtue of the articles. They are not exercising a delegated power. They have an original power to manage the company, conferred by the Act, except to the extent that that power is modified, excluded or limited by the constitution of the company or the Act.

Thus it seems to me that an ad hoc resolution of shareholders to approve or ratify a board decision provides no legal protection to directors: indeed if this is true where the approval is given pursuant to a requirement in the constitution, it is *a fortiori* true of ad hoc decisions.

Shareholder decision making – no constitutional provision

The position is essentially the same where shareholders purport to make a decision that the company should enter into a particular transaction or do some other act, in circumstances where this is not required by the Act, and the constitution does not provide for shareholders to decide that matter. In my view it is likely that such a decision has no legal effect. At most, it is possible that a Court might consider that it had some evidential value in respect of certain types of claim by a company, in circumstances where the company was solvent at the time the resolution was passed, and was expected to remain solvent after the transaction in question.

The significant difference in legal consequences between a shareholder decision that is provided for in the constitution, and one that is not provided for in the constitution, means that if directors are looking for a high degree of legal protection it would be prudent to first amend the constitution to provide for shareholder decision making on the issue in question, and then pass a resolution pursuant to that constitutional provision approving the transaction in question. Amending the constitution will of course require a special resolution. (Whether

shareholders fully informed of the legal implications of such a course will agree to it is, of course, another matter!)

Ratification of breaches of duty after the event
This topic overlaps with the general ad hoc approval/ratification discussion above. The old rule that shareholders could ratify a decision of directors and thus preclude a claim by the company against the directors is difficult to apply to 1993 Act companies, though it is often assumed that it continues to apply. The decision on whether or not to bring proceedings is a management decision, not a shareholder decision. So it is for the directors to make. Unless the constitution of the company authorises shareholders to make this decision, I cannot see any basis for concluding that a ratification by shareholders is effective to exclude the ability to bring proceedings.

Despite the promising title of section 177 – "ratification of certain actions of directors" – the provision sheds no light on this issue. It confirms only that if the directors exercise a power vested in shareholders or some other person, the shareholders or other person can ratify the exercise of the power. But where the power was always a board power, as with the power to manage the company, section 177 simply does not apply. Subsection (4) reads more as a provision included out of an abundance of caution than as a deliberate preservation of all of the pre-1993 caselaw; and to the extent that that caselaw is inconsistent with **other** provisions of the 1993 Act, or indeed its basic structure and allocation of powers, s177(4) is of no assistance at all.[11]

The closest the 1993 Act comes to a positive suggestion that the shareholders can decide whether or not to ratify steps taken by directors is in section 165(3), in relation to derivative actions. The Court can grant leave to a shareholder or director to bring or intervene in proceedings only if the Court is satisfied that, among other things, it is in the interests of the company that the conduct of the proceedings should not be left to the directors or *to the determination of the*

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[11] For a helpful discussion of the pre-1993 caselaw see Rennie & Watts op cit pp71-72; *Morison* para 25.44.

shareholders as a whole. But this is a rather slender foundation on which to build a general power to ratify.

Overview

The above discussion highlights a number of pitfalls and inconsistencies in the Act's treatment of shareholder decision making. The consequences for both directors and shareholders vary dramatically depending on the contents of the company's constitution and the nature of the shareholder decision. It is surprisingly difficult to work out just what the consequences are, in some cases. And the directors obtain much less protection from shareholder approval than is sometimes believed to be the case.

It seems to me that there is a strong case for clarifying the effect of shareholder decision making and shareholder approval of various matters, and for seeking to achieve a greater measure of consistency in how shareholder participation in management affects the responsibilities of the directors.

Where a company is solvent, there is in my view a strong policy argument that shareholder approval should be conclusive so far as the duty to act in good faith and in the interests of the company, the duty to exercise a power for a proper purpose, and the section 137 duty of care are concerned. The basic policy argument is that if the company is solvent both before and after the transaction is entered into, the shareholders are the owners of the assets that are being dealt with, and should be able to agree to a dealing in respect of those assets. No one else has any interest in how they are dealt with. So unanimous shareholder approval of a transaction should certainly be sufficient, and in my view a majority approval should also be sufficient, subject to the various protections in terms of interested transactions, major transactions and unfairly prejudicial conduct that are already provided for elsewhere in the Act.

If on the other hand the company is insolvent, or its solvency is doubtful, the policy justification for permitting directors to rely on shareholder approval is much weaker. The risks they are taking are not risks with the shareholders' money, but rather with the money of creditors. From a policy perspective, it seems to me that if the directors know or ought to know that the company is

insolvent, they should not be able to rely on shareholder approval to validate conduct that would otherwise be unauthorised, or a breach of duty to the company. In a number of cases the High Court has made comments to the effect that shareholder approval does not cure breaches of duties to creditors, without engaging in any detailed analysis as to why this should be so. Note moreover that this argument extends not only to the duties specifically concerned with reckless trading and ability to perform obligations (sections 135 and 136), but also to more general duties to the company such as the duty to act in its best interests. Shareholders whose money is not in issue should not be able to authorise directors to disregard the interests of the company, when it is being funded solely with creditors' money.

Until such reforms occur, it is important for directors and their advisers to be aware of the different implications of different mechanisms for seeking shareholder approval. For directors, the most attractive option is to seek to amend the company's constitution to provide for the decision to be made by shareholders. If the technique is likely to be used regularly by a company, it may be desirable to include in the constitution a general provision to the effect that the directors may refer any matter to shareholders for determination, and that matters referred under this provision will be decided on by shareholders, and not by directors.

For shareholders, however, this approach contains many pitfalls as they come under a wide range of duties in respect of how they vote, and risk liability to creditors.

The least satisfactory approach appears to be for directors to decide on a matter, then seek shareholder approval of that decision. If this is done pursuant to a constitutional provision, both directors and shareholders will probably be liable. If it is done on an ad hoc basis, shareholders probably escape liability, but it is far from clear that directors are in a materially better position than if the approval had not been sought: it has some evidential value, at best.

Directors' duties: some issues

The discussion thus far has taken the duties of directors in the 1993 Act as given, and looked at the consequences for those duties of shareholder decision making and approvals. But there are some serious defects in the directors' duties provisions of the 1993 Act which exacerbate those concerns.

Mandatory versus default provisions

Perhaps the most fundamental problem with the director duty provisions of the 1993 Act is that they are all drafted as mandatory provisions: it seems most unlikely that they can be modified or excluded by the company constitution, in sharp contrast with the legal position of managing partners in a partnership, or trustees of a unit trust, for example. Putting to one side the basic fiduciary obligations to act in good faith and avoid undisclosed self-dealing, and the creditor/solvency duties in sections 135 and 136, it seems to me that all of the remaining obligations of directors should be capable of being modified or excluded by the company constitution. This would enable companies to tailor appropriate arrangements for their circumstances, and would significantly reduce the risk of setting the wrong standard in the Act itself in relation to matters such as the duty of care of directors. The Companies Act 2001 of Samoa (which I drafted) attempts to give effect to this basic approach, and allow shareholders to agree to modify certain director duties, either in the constitution or through other forms of approval or acquiescence, provided the company is solvent. Some of the relevant provisions of that Act are set out in appendix 2 to this paper. I have discussed this issue in more detail elsewhere: see "Company Law Reform – Lessons from the New Zealand Experience" in Borrowdale, Rowe and Taylor (eds) *Company Law Writings – A New Zealand Collection* (Centre for Commercial and Corporate Law, University of Canterbury, 2002).

"Proper purpose": s133 should be repealed

Turning to the particular duties prescribed by the Act, the most problematic is in my view section 133, which requires powers to be exercised for a proper purpose. I simply do not know what this adds to the obligation to act in good faith and in what the director believes to be the best interests of the company. This provision, which was inserted into the Companies Bill at the Select Committee stage, takes

some case law which formulated an obligation along these lines in the limited context of share issues affecting the control of the company, and turns it into a duty of general application.[12] I have never yet seen a satisfactory account of what it might mean as a generally applicable duty, over and above sections 131 and 137, and the specific statutory regimes that now govern share issues and repurchases. It should in my view be repealed.

Unless and until this provision is deleted, it seems to me that as with so many provisions of the 1993 Act, the best protection for directors is to record the purpose for which a power is being exercised, in circumstances where that is or may become a matter of controversy. Provided a company is solvent, the argument that a power is being exercised for a proper purpose is also in my view substantially strengthened by approval, formal or informal, from shareholders.

Section 134 strict liability

I have written elsewhere about directors' strict liability for acting inconsistently with the requirements of the Act, or the company's constitution.[13] The provision is unobjectionable, but should in my view be accompanied by provisions:

- excluding liability for breach of the constitution, where the action in question has been approved by all shareholders, or (perhaps) by a special resolution;

- permitting companies to specify in their constitutions that directors are not liable for breaches of certain duties, including the obligation to act consistently with the constitution, if they act honestly and reasonably. Such provisions are found in many trust deeds – why not in company constitutions, if that is what the shareholders want?

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[12] See the excellent discussion of the cases, and the relationship between the caselaw and s133, in Hugh Rennie & Peter Watts, *Directors' Duties and Shareholders' Rights* (NZLS Seminar, 1996).

[13] "Strict Liability of Directors: When Acting Reasonably – Or On Advice – Is Not Enough" [1999] CSLB 118.

Sections 135 and 136 should be repealed

Sections 135 and 136 are in my view equally flawed. I cannot discuss them in detail, in the time available today. I have discussed elsewhere the reasons why these provisions (and also section 300) should be repealed.[14] I have suggested replacing them with a provision imposing liability to creditors for culpable non disclosure that the company is insolvent and unable to perform an obligation which it is assuming[15], and possibly (depending on further analysis) with an additional provision imposing liability to the company for net losses incurred as a result of trading on after the directors knew (or should have known) that the company was insolvent, or as a result of taking certain excessive risks in specified financial circumstances. I do not think there is any principled basis for a more extensive imposition of liability in this area.

Meanwhile, there is not much that directors can do to minimise their exposure under sections 135, 136 and 300. Shareholder approval certainly will not help. The most that can be done is to create a paper trail which demonstrates that directors have turned their mind to solvency matters, and formed a view in good faith and on reasonable grounds. This is easy to say. But it can be time consuming and costly to do.

"Best" interests of the company

A less significant but nonetheless important quibble concerns section 131 itself. Directors are required to act in what they believe to be the *best* interests of the company.[16] The better view is that pre-1993, the obligation was to act in what the directors believed to be the interests of the company. That is, they were required

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[14] "Directors' Liability for Trading While Insolvent: A Critical Review of the New Zealand Regime" in Ian Ramsay (ed), *Company Directors' Liability for Insolvent Trading* (Centre for Corporate Law and Securities Regulation, University of Melbourne, 2000).

[15] For an argument that such non-disclosure can give rise to a cause of action under the existing law, see *Cripps and Others v Traveller & Fisk* (unreported, High Court, Wellington Registry CIV-2003-485-1616, 30 June 2004, Mackenzie J) paras 72-81.

[16] For a helpful discussion of who is to be regarded as "the company" for s131 purposes, and the extent to which this re-imports the caselaw on the circumstances in which directors must take into account the interests of creditors, see *Rennie & Watts* op at pp12-21. That duties to the company require a consideration of the interests of creditors, in the case of a company of marginal solvency, was accepted by Young J in *Re Mako Holdings Ltd* (unreported, High Court, Invercargill Registry CP No 23/99, 28 November, Young J).

to satisfy themselves that the company would benefit from the decision they were making. They were not required to be satisfied that there was nothing better that could be done. Yet that is, at least on its face, what section 131 requires. I am not aware of any policy case having been made out for raising the bar in this way, and it seems to me unrealistic to say that directors cannot approve a transaction if they are satisfied that it will benefit the company, but are not satisfied that there is nothing else that could have been done that would be more beneficial still.

In other jurisdictions where I have been involved in company law reform projects, I have recommended enacting a version of section 131 that omits the word "best".

Section 137 – the reasonable director

I also have some concerns in relation to the drafting of section 137, which requires a director to exercise the care, diligence and skill that a reasonable director would exercise in the same circumstances, taking into account certain matters. I am not sure that I know what a reasonable director looks like, or how one would go about calling evidence on what a reasonable director of a small, closely held company would do in certain circumstances. But my concerns in relation to this provision are probably better addressed not by altering the provision itself, but rather by permitting the standard it sets to be modified by the constitution of the company, if shareholders so agree.

Delegation by directors

Section 130 provides for the delegation of powers by directors. The delegate becomes a deemed director for the purposes of sections 131 to 149, 298, 299, 301, 383 and 385 (section 126(1)(c)). Section 130 also imposes liability on the board for the exercise of the power by the delegate, as if it had been exercised by the board, unless certain stringent conditions are met. Section 130 reverses the common law onus in relation to delegation by directors and relies on information and advice provided to directors by other directors, employees and advisers. For example, the Act requires directors to have reasonable grounds for believing that a delegate would exercise a power in conformity with the duties imposed on directors of the company by the Act and the company's constitution, and requires the exercise of powers to be monitored appropriately. And it requires directors to

have reasonable grounds for believing that an employee who provides information is reliable and competent in relation to the matters concerned, and that a professional or expert adviser is giving advice within their professional or expert competence.

It is far from obvious what directors must inquire into and learn in order to have reasonable grounds for trusting the various providers of information and advice on whom they routinely rely. Nor is it obvious what additional inquiries must be made in relation to senior employees such as the chief executive or CFO, before delegating powers to them and trusting them to exercise those powers. If the person is trusted to perform their duties generally, what more is required?

It would make much more sense, and would be consistent with established legal principles and commercial reality, to provide that directors can rely on information and advice unless they have grounds for believing that the provider is not reliable or competent. Similarly, the board should be responsible for exercise of powers by a delegate only if the board is, or should be, aware that the person is acting or is likely to act improperly.

Various strategies can be adopted to minimise risk to directors from delegations. In any initial delegations, there should probably be an express provision that the delegate acknowledges that he or she is required to exercise the power in conformity with the duties of directors under the Act and the constitution, and agrees to do so. The delegation can provide that unless and until this acknowledgement is given, the delegation is ineffective. Having received this initial assurance, monitoring mechanisms can be put in place to ensure that if powers are improperly exercised, that is likely to come to the attention of the board. It is not easy to see what more can be done.

And a board is in a particularly invidious position where it begins to develop concerns about the performance of a chief executive or other senior executive, but wishes to explore those concerns and ensure they are justified before taking precipitate action: in such circumstances the risks under section 130 are very acute, and the incentives created by section 130 appear directly at odds with much of the thrust of New Zealand’s employment legislation.

For smaller companies, the same technique of requiring delegates to acknowledge that they are required to exercise their powers in accordance with the duties of directors under the Act and the constitution is reasonably simple and low cost. Whether it is likely to occur in practice, in circumstances where most delegations are reasonably informal, is another matter. There is no case law, as yet, on what would amount to monitoring the exercise of delegated power, by means of reasonable methods properly used, in the context of a small or medium sized company. It is to be hoped that a commercially realistic approach will be adopted by the Courts, under which a reasonable level of reporting by the delegate in question, and fairly lighthanded supervision by the board, will be seen as adequate.

Some proposals for reform

In the remaining time, let me make some suggestions for reform that would address the principal concerns I have identified today. There are three basic paths that such reform could, in my view, take.

The first would be to revisit, in a fairly fundamental way, the manner in which the 1993 Act approaches the relationship between shareholders and directors. A contractual/agency paradigm could be restored to the Act, many of the existing mandatory rules would be recast as default rules, and a number of the more problematic provisions could be repealed or substantially amended.

This approach is perhaps the most theoretically pure. But it seems to me unlikely that it will be adopted in practice. The experience of company law reform in New Zealand in the early 1990s suggests that there is significant opposition to more facilitative company law, especially so far as larger companies are concerned. The distinction between company law, securities law and the law relating to listed companies was emphasised by the Law Commission, but was lost sight of at a number of stages in the course of these reforms. Concerns about the management of larger companies influenced a number of the provisions I have discussed today, and resulted in their being framed in terms that are inappropriate for smaller companies.

A second, less far reaching approach would be to tidy up some of the inconsistencies identified in this paper, and make clearer provision for the effect of provisions in the constitution in relation to shareholder management and director duties, and clearer provision for the effect of shareholder approvals and decision making external to the constitution. Provided that a number of the provisions in respect of which I have expressed reservations are treated as default provisions, capable of modification in the constitution of a company, my concerns would be substantially reduced.

The third and perhaps most promising approach would however be to enact a separate, much simplified, Closely Held Companies Act. Such an Act could look as much to partnership law as to company law, especially so far as the internal dealings of shareholders and directors are concerned. A clear distinction would be drawn between mandatory provisions concerning dealings with third parties, and default provisions concerning the internal management of the company. Most if not all of the difficulties I have identified above could be avoided. And, because the Act would focus on closely held companies, many of the factors that drove increased complexity and rigidity in the 1993 Act would, hopefully, be avoided.

Such an Act would also contribute to the Government’s objective of reducing unnecessary transaction costs for SMEs, and encouraging economic development and entrepreneurship in New Zealand.

Appendix 1: Companies Act 1993, ss126-149

126. Meaning of “director”'—

(1) In this Act, “director'”, in relation to a company, includes—

(a) A person occupying the position of director of the company by whatever name called; and

(b) For the purposes of sections 131 to 141, 145 to 149, 298, 299, [301, 383, [[385, and clause 12(ab) of Schedule 7]]],—

(i) A person in accordance with whose directions or instructions a person referred to in paragraph (a) of this subsection may be required or is accustomed to act; and

(ii) A person in accordance with whose directions or instructions the board of the company may be required or is accustomed to act; and

(iii) A person who exercises or who is entitled to exercise or who controls or who is entitled to control the exercise of powers which, apart from the constitution of the company, would fall to be exercised by the board; and

(c) For the purposes of sections 131 to 149, 298, 299, [301, 383, [[[[[385, and clause 12(ab) of Schedule 7]]]]]], a person to whom a power or duty of the board has been directly delegated by the board with that person's consent or acquiescence, or who exercises the power or duty with the consent or acquiescence of the board; and

(d) For the purposes of sections 145 to 149[, and clause 12(ab) of Schedule 7] of this Act, a person in accordance with whose directions or instructions a person referred to in paragraphs (a) to (c) of this subsection may be required or is accustomed to act in respect of his or her duties and powers as a director.

[(1A) In this Act, ``director'', in relation to a company, does not include a receiver.]

(2) If the constitution of a company confers a power on shareholders which would otherwise fall to be exercised by the board, any shareholder who exercises that power or who takes part in deciding whether to exercise that power is deemed, in relation to the exercise of the power or any consideration concerning its exercise, to be a director for the purposes of sections 131 to 138 of this Act.

(3) If the constitution of a company requires a director or the board to exercise or refrain from exercising a power in accordance with a decision or direction of shareholders, any shareholder who takes part in—

(a) The making of any decision that the power should or should not be exercised; or

(b) The making of any decision whether to give a direction,—

as the case may be, is deemed, in relation to making any such decision, to be a director for the purposes of sections 131 to 138 of this Act.

(4) Paragraphs (b) to (d) of subsection (1) of this section do not include a person to the extent that the person acts only in a professional capacity.

127. Meaning of ``board"—

In this Act, the terms ``board" and ``board of directors", in relation to a company, mean—

(a) Directors of the company who number not less than the required quorum acting together as a board of directors; or

(b) If the company has only one director, that director.

Powers of management

128. Management of company—

(1) The business and affairs of a company must be managed by, or under the direction or supervision of, the board of the company.

(2) The board of a company has all the powers necessary for managing, and for directing and supervising the management of, the business and affairs of the company.

(3) Subsections (1) and (2) of this section are subject to any modifications, exceptions, or limitations contained in this Act or in the company's constitution.

129. Major transactions—

(1) A company must not enter into a major transaction unless the transaction is—

(a) Approved by special resolution; or

(b) Contingent on approval by special resolution.

(2) In this section,—

``Assets" includes property of any kind, whether tangible or intangible;

[``Major transaction", in relation to a company, means:

(a) The acquisition of, or an agreement to acquire, whether contingent or not, assets the value of which is more than half the value of the company's assets before the acquisition; or

(b) The disposition of, or an agreement to dispose of, whether contingent or not, assets of the company the value of which is more than half the value of the company's assets before the disposition; or

(c) A transaction that has or is likely to have the effect of the company acquiring rights or interests or incurring obligations or liabilities[[, including contingent liabilities,]] the value of which is more than half the value of the company's assets before the transaction.]

[(2A) Nothing in [[paragraph (b) or]] paragraph (c) of the definition of the term ``major transaction" in subsection (2) of this section applies by reason only of the company giving, or entering into an agreement to give, a . . . charge secured over assets of the company the value of which is more than half the value of the company's assets for the purpose of securing the repayment of money or the performance of an obligation.]

[(2B) In assessing the value of any contingent liability for the purposes of paragraph (c) of the definition of ``major transaction" in subsection (2), the directors—

(a) must have regard to all circumstances that the directors know, or ought to know, affect, or may affect, the value of the contingent liability; and

(b) may rely on estimates of the contingent liability that are reasonable in the circumstances; and

(c) may take account of—

(i) the likelihood of the contingency occurring; and

(ii) any claim the company is entitled to make and can reasonably expect to be met to reduce or extinguish the contingent liability.]

(3) Nothing in this section applies to a major transaction entered into by a receiver appointed pursuant to an instrument creating a charge over all or substantially all of the property of a company.

130. Delegation of powers—

(1) Subject to any restrictions in the constitution of the company, the board of a company may delegate to a committee of directors, a director or employee of the company, or any other person, any one or more of its powers other than its powers under any of the sections of this Act set out in Schedule 2 to this Act.

(2) A board that delegates a power under subsection (1) of this section is responsible for the exercise of the power by the delegate as if the power had been exercised by the board, unless the board—

(a) Believed on reasonable grounds at all times before the exercise of the power that the delegate would exercise the power in conformity with the duties imposed on directors of the company by this Act and the company's constitution; and

(b) Has monitored, by means of reasonable methods properly used, the exercise of the power by the delegate.

Directors' duties

131. Duty of directors to act in good faith and in best interests of company—

(1) Subject to this section, a director of a company, when exercising powers or performing duties, must act in good faith and in what the director believes to be the best interests of the company.

(2) A director of a company that is a wholly-owned subsidiary may, when exercising powers or performing duties as a director, if expressly permitted to do so by the constitution of the company, act in a manner which he or she believes is in the best interests of that company's holding company even though it may not be in the best interests of the company.

(3) A director of a company that is a subsidiary (but not a wholly-owned subsidiary) may, when exercising powers or performing duties as a director, if expressly permitted to do so by the constitution of the company and with the prior agreement of the shareholders (other than its holding company), act in a manner which he or she believes is in the best interests of that company's holding company even though it may not be in the best interests of the company.

(4) A director of a company [that is carrying] out a joint venture between the shareholders may, when exercising powers or performing duties as a director in connection with the carrying out of the joint venture, if expressly permitted to do so by the constitution of the company, act in a manner which he or she believes is in the best

interests of a shareholder or shareholders, even though it may not be in the best interests of the company.

132. Exercise of powers in relation to employees—

(1) Nothing in section 131 of this Act limits the power of a director to make provision for the benefit of employees of the company in connection with the company ceasing to carry on the whole or part of its business.

(2) In subsection (1) of this section,—

“`Employees” includes former employees and the dependants of employees or former employees; but does not include an employee or former employee who is or was a director of the company:

“Company” includes a subsidiary of a company.

133. Powers to be exercised for proper purpose—

A director must exercise a power for a proper purpose.

134. Directors to comply with Act and constitution—

A director of a company must not act, or agree to the company acting, in a manner that contravenes this Act or the constitution of the company.

135. Reckless trading—

A director of a company must not—

(a) Agree to the business of the company being carried on in a manner likely to create a substantial risk of serious loss to the company's creditors; or

(b) Cause or allow the business of the company to be carried on in a manner likely to create a substantial risk of serious loss to the company's creditors.

136. Duty in relation to obligations—

A director of a company must not agree to the company incurring an obligation unless the director believes at that time on reasonable grounds that the company will be able to perform the obligation when it is required to do so.

137. Director's duty of care—

A director of a company, when exercising powers or performing duties as a director, must exercise the care, diligence, and skill that a reasonable director would exercise in the same circumstances taking into account, but without limitation,—

(a) The nature of the company; and

(b) The nature of the decision; and

(c) The position of the director and the nature of the responsibilities undertaken by him or her.

138. Use of information and advice—

(1) Subject to subsection (2) of this section, a director of a company, when exercising powers or performing duties as a director, may rely on reports, statements, and

financial data and other information prepared or supplied, and on professional or expert advice given, by any of the following persons:

(a) An employee of the company whom the director believes on reasonable grounds to be reliable and competent in relation to the matters concerned:

(b) A professional adviser or expert in relation to matters which the director believes on reasonable grounds to be within the person's professional or expert competence:

(c) Any other director or committee of directors upon which the director did not serve in relation to matters within the director's or committee's designated authority.

(2) Subsection (1) of this section applies to a director only if the director—

(a) Acts in good faith; and

(b) Makes proper inquiry where the need for inquiry is indicated by the circumstances; and

(c) Has no knowledge that such reliance is unwarranted.

Transactions involving self-interest

139. Meaning of ``interested''—

(1) Subject to subsection (2) of this section, for the purposes of this Act, a director of a company is interested in a transaction to which the company is a party if, and only if, the director—

(a) Is a party to, or will or may derive a material financial benefit from, the transaction; or

(b) Has a material financial interest in another party to the transaction; or

(c) Is a director, officer, or trustee of another party to, or person who will or may derive a material financial benefit from, the transaction, not being a party or person that is—

(i) The company's holding company being a holding company of which the company is a wholly-owned subsidiary; or

(ii) A wholly-owned subsidiary of the company; or

(iii) A wholly-owned subsidiary of a holding company of which the company is also a wholly-owned subsidiary; or

(d) Is the parent, child, or spouse of another party to, or person who will or may derive a material financial benefit from, the transaction; or

(e) Is otherwise directly or indirectly materially interested in the transaction.

(2) For the purposes of this Act, a director of a company is not interested in a transaction to which the company is a party if the transaction comprises only the giving by the company of security to a third party which has no connection with the director, at the request of the third party, in respect of a debt or obligation of the company for which

the director or another person has personally assumed responsibility in whole or in part under a guarantee, indemnity, or by the deposit of a security.

140. Disclosure of interest—

(1) A director of a company must, forthwith after becoming aware of the fact that he or she is interested in a transaction or proposed transaction with the company, cause to be entered in the interests register, and, if the company has more than one director, disclose to the board of the company—

(a) If the monetary value of the director's interest is able to be quantified, the nature and monetary value of that interest; or

(b) If the monetary value of the director's interest cannot be quantified, the nature and extent of that interest.

[(1A) A director of a company is not required to comply with subsection (1) if—

(a) The transaction or proposed transaction is between the director and the company; and

(b) The transaction or proposed transaction is or is to be entered into in the ordinary course of the company's business and on usual terms and conditions.]

(2) For the purposes of subsection (1) of this section, a general notice entered in the interests register [and, if the company has more than 1 director,] disclosed to the board to the effect that a director is a shareholder, director, officer or trustee of another named company or other person and is to be regarded as interested in any transaction which may, after the date of the entry or disclosure, be entered into with that company or person, is a sufficient disclosure of interest in relation to that transaction.

(3) A failure by a director to comply with subsection (1) of this section does not affect the validity of a transaction entered into by the company or the director.

(4) Every director who fails to comply with subsection (1) of this section commits an offence and is liable on conviction to the penalty set out in section 373(2) of this Act.

141. Avoidance of transactions—

(1) A transaction entered into by the company in which a director of the company is interested may be avoided by the company at any time before the expiration of 3 months after the transaction is disclosed to all the shareholders (whether by means of the company's annual report or otherwise).

(2) A transaction cannot be avoided if the company receives fair value under it.

(3) For the purposes of subsection (2) of this section, the question whether a company receives fair value under a transaction is to be determined on the basis of the information known to the company and to the interested director at the time the transaction is entered into.

(4) If a transaction is entered into by the company in the ordinary course of its business and on usual terms and conditions, the company is presumed to receive fair value under the transaction.

(5) For the purposes of this section,—

(a) A person seeking to uphold a transaction and who knew or ought to have known of the director's interest at the time the transaction was entered into has the onus of establishing fair value; and

(b) In any other case, the company has the onus of establishing that it did not receive fair value.

(6) A transaction in which a director is interested can only be avoided on the ground of the director's interest in accordance with this section or the company's constitution.

142. Effect on third parties—

The avoidance of a transaction under section 141 of this Act does not affect the title or interest of a person in or to property which that person has acquired if the property was acquired—

(a) From a person other than the company; and

(b) For valuable consideration; and

(c) Without knowledge of the circumstances of the transaction under which the person referred to in paragraph (a) of this section acquired the property from the company.

143. Application of sections 140 and 141 in certain cases—

Nothing in section 140 and section 141 of this Act applies in relation to—

(a) Remuneration or any other benefit given to a director in accordance with section 161 of this Act; or

(b) An indemnity given or insurance provided in accordance with section 162 of this Act.

144. Interested director may vote—

Subject to the constitution of the company, a director of a company who is interested in a transaction entered into, or to be entered into, by the company, may—

(a) Vote on a matter relating to the transaction; and

(b) Attend a meeting of directors at which a matter relating to the transaction arises and be included among the directors present at the meeting for the purpose of a quorum; and

(c) Sign a document relating to the transaction on behalf of the company; and

(d) Do any other thing in his or her capacity as a director in relation to the transaction—

as if the director were not interested in the transaction.

145. Use of company information—

(1) A director of a company who has information in his or her capacity as a director or employee of the company, being information that would not otherwise be available to him or her, must not disclose that information to any person, or make use of or act on the information, except—

(a) For the purposes of the company; or

(b) As required by law; or

(c) In accordance with subsection (2) or subsection (3) of this section; or

(d) In complying with section 140 of this Act.

(2) A director of a company may, unless prohibited by the board, disclose information to—

(a) A person whose interests the director represents; or

(b) A person in accordance with whose directions or instructions the director may be required or is accustomed to act in relation to the director's powers and duties and, if the director discloses the information, the name of the person to whom it is disclosed must be entered in the interests register.

(3) A director of a company may disclose, make use of, or act on the information if—

(a) Particulars of the disclosure, use, or the act in question are entered in the interests register; and

(b) The director is first authorised to do so by the board; and

(c) The disclosure, use, or act in question will not, or will not be likely to, prejudice the company.

146. Meaning of ``relevant interest''—

(1) For the purposes of section 148 of this Act, a director of a company has a relevant interest in a share issued by a company (whether or not the director is registered in the share register as the holder of it) if the director—

(a) Is a beneficial owner of the share; or

(b) Has the power to exercise any right to vote attached to the share; or

(c) Has the power to control the exercise of any right to vote attached to the share; or

(d) Has the power to acquire or dispose of the share; or

(e) Has the power to control the acquisition or disposition of the share by another person; or

(f) Under, or by virtue of, any trust, agreement, arrangement or understanding relating to the share (whether or not that person is a party to it)—

(i) May at any time have the power to exercise any right to vote attached to the share; or

(ii) May at any time have the power to control the exercise of any right to vote attached to the share; or

(iii) May at any time have the power to acquire or dispose of, the share; or

(iv) May at any time have the power to control the acquisition or disposition of the share by another person.

(2) Where a person [would, if that person were a director of the company, have] a relevant interest in a share by virtue of subsection (1) of this section and—

(a) That person or its directors are accustomed or under an obligation, whether legally enforceable or not, to act in accordance with the directions, instructions, or wishes of a director of the company in relation to—

(i) The exercise of the right to vote attached to the share; or

(ii) The control of the exercise of any right to vote attached to the share; or

(iii) The acquisition or disposition of the share; or

(iv) The exercise of the power to control the acquisition or disposition of the share by another person; or

(b) A director of the company has the power to exercise the right to vote attached to 20 percent or more of the shares of that person; or

(c) A director of the company has the power to control the exercise of the right to vote attached to 20 percent or more of the shares of that person; or

(d) A director of the company has the power to acquire or dispose of 20 percent or more of the shares of that person; or

(e) A director of the company has the power to control the acquisition or disposition of 20 percent or more of the shares of that person,—

that director has a relevant interest in the share.

(3) A person who has, or may have, a power referred to in any of paragraphs (b) to (f) of subsection (1) of this section, has a relevant interest in a share regardless of whether the power—

(a) Is expressed or implied:

(b) Is direct or indirect:

(c) Is legally enforceable or not:

(d) Is related to a particular share or not:

(e) Is subject to restraint or restriction or is capable of being made subject to restraint or restriction:

(f) Is exercisable presently or in the future:

(g) Is exercisable only on the fulfilment of a condition:

(h) Is exercisable alone or jointly with another person or persons.

(4) A power referred to in subsection (1) of this section exercisable jointly with another person or persons is deemed to be exercisable by either or any of those persons.

(5) A reference to a power includes a reference to a power that arises from, or is capable of being exercised as the result of, a breach of any trust, agreement, arrangement, or understanding, or any of them, whether or not it is legally enforceable.

147. Relevant interests to be disregarded in certain cases—

(1) For the purposes of section 148 of this Act, no account shall be taken of a relevant interest of a person in a share if—

(a) The ordinary business of the person who has the relevant interest consists of, or includes, the lending of money or the provision of financial services, or both, and that person has the relevant interest only as security given for the purposes of a transaction entered into in the ordinary course of the business of that person; or

(b) That person has the relevant interest by reason only of acting for another person to acquire or dispose of that share on behalf of the other person in the ordinary course of business of a sharebroker and that person is a [person authorised to undertake trading activities on] a stock exchange; or

(c) That person has the relevant interest solely by reason of being appointed as a proxy to vote at a particular meeting of members, or of a class of members, of the company and the instrument of that person's appointment is produced before the start of the meeting in accordance with clause 6(4) of Schedule 1 to this Act or by a time specified in the company's constitution, as the case may be; or

(d) That person—

(i) Is a trustee corporation or a nominee company; and

(ii) Has the relevant interest by reason only of acting for another person in the ordinary course of business of that trustee corporation or nominee company; or

(e) The person has the relevant interest by reason only that the person is a bare trustee of a trust to which the share is subject.

(2) For the purposes of subsection (1)(e) of this section, a trustee may be a bare trustee notwithstanding that he or she is entitled as a trustee to be remunerated out of the income or property of the trust.

148. Disclosure of share dealing by directors—

(1) A director of a company that has become registered under this Act in accordance with the Companies Reregistration Act 1993 and who has a relevant interest in any shares issued by the company must, forthwith after the reregistration of the company,—

(a) Disclose to the board the number and class of shares in which the relevant interest is held and the nature of the relevant interest; and

(b) Ensure that the particulars disclosed to the board under paragraph (a) of this subsection are entered in the interests register.

(2) A director of a company who acquires or disposes of a relevant interest in shares issued by the company must, forthwith after the acquisition or disposition,—

(a) Disclose to the board—

(i) The number and class of shares in which the relevant interest has been acquired or the number and class of shares in which the relevant interest was disposed of, as the case may be; and

(ii) The nature of the relevant interest; and

(iii) The consideration paid or received; and

(iv) The date of the acquisition or disposition; and

(b) Ensure that the particulars disclosed to the board under paragraph (a) of this subsection are entered in the interests register.

149. Restrictions on share dealing by directors—

(1) If a director of a company has information in his or her capacity as a director or employee of the company or a related company, being information that would not otherwise be available to him or her, but which is information material to an assessment of the value of shares or other securities issued by the company or a related company, the director may acquire or dispose of those shares or securities only if,—

(a) In the case of an acquisition, the consideration given for the acquisition is not less than the fair value of the shares or securities; or

(b) In the case of a disposition, the consideration received for the disposition is not more than the fair value of the shares or securities.

(2) For the purposes of subsection (1) of this section, the fair value of shares or securities is to be determined on the basis of all information known to the director or publicly available at the time.

(3) Subsection (1) of this section does not apply in relation to a share or security that is acquired or disposed of by a director only as a nominee for the company or a related company.

(4) Where a director acquires shares or securities in contravention of subsection (1)(a) of this section, the director is liable to the person from whom the shares or securities were acquired for the amount by which the fair value of the shares or securities exceeds the amount paid by the director.

(5) Where a director disposes of shares or securities in contravention of subsection (1)(b) of this section, the director is liable to the person to whom the shares or securities were disposed of for the amount by which the consideration received by the director exceeds the fair value of the shares or securities.

(6) Nothing in this section applies in relation to a company to which Part 1 of the Securities [Markets] Amendment Act 1988 applies.

Appendix 2: Companies Act 2001 (Samoa) – extracts

PART FIVE

SHAREHOLDERS AND THEIR RIGHTS AND OBLIGATIONS

Liability of shareholders

43. Liability of shareholders - (1) A shareholder is not liable for an obligation of the company by reason only of being a shareholder**.**

(2) The liability of a shareholder to the company is limited to –

(a) any liability to repay a distribution which is recoverable under section 23;

(b) any liability under section 71.

(3) Nothing in this section affects the liability of a shareholder to a company under a contract, including a contract for the issue of shares, or liability incurred in any other capacity, including as a director of the company, or liability for any tort, or breach of a fiduciary duty, or other actionable wrong committed by the shareholder.

Powers of shareholders

44. Decisions which must be made by shareholders - The following powers must be exercised by the shareholders of a company by special resolution, and may not be delegated under the Articles or otherwise:

(a) the power to approve re-registration of a public company as a private company under section 9(3), or of a private company as a public company under section 9(4);

(b) the power to adopt new Articles, or to amend the company's Articles, under section 14(2);

(c) the power to approve an amalgamation of the company under section 121 and the Fifth Schedule;

(d) the power to approve a major transaction under section 46(1)(b)(i);

(e) the power to put the company into liquidation;

(f) the power to approve an extension of time for the completion of a private company's financial statements under section 111(3);

(g) the power to approve the transfer of registration of the company to another country under section 173.

45. Decisions which may be made by shareholders - (1) Unless the Articles provide otherwise, the following powers are exercised by shareholders:

(a) the power to appoint or remove a director;

(b) the power to appoint an auditor.

(2) The Articles may provide for other matters to be decided by shareholders, or approved by shareholders.

(3) Unless the Articles provide otherwise, the powers referred to in subsection (1), and any other powers conferred on shareholders under subsection (2), may be exercised –

(a) by ordinary resolution; or

(b) in accordance with section 47.

46. Shareholder approval of major transactions - (1) A company must not enter into a major transaction unless –

(a) the Articles expressly authorise it to enter into that transaction, or transactions of that class; or

(b) entry into the transaction is approved by shareholders –

(i) by special resolution; or

(ii) in accordance with section 47; or

(c) the transaction is conditional on approval by shareholders in accordance with paragraph (b).

(2) In this section:

"**Assets**" includes property of any kind, whether tangible or intangible;

"**Major transaction**", in relation to a company, means:

(a) the acquisition of, or an agreement to acquire, whether contingent or not, assets the value of which is more than half the value of the company's assets before the acquisition; or

(b) the disposition of, or an agreement to dispose of, whether contingent or not, assets of the company the value of which is more than half the value of the company's assets before the disposition; or

(c) a transaction that has or is likely to have the effect of the company acquiring rights or interests or incurring obligations or liabilities the value of which is more than half the value of the company's assets before the transaction.

(3) Nothing in paragraph (c) of the definition of the term "major transaction" in subsection (2) applies by reason only of the company giving, or entering into an agreement to give, a charge secured over assets of the company the value of which is more than half the value of the company's assets for the purpose of securing the repayment of money or the performance of an obligation.

(4) Nothing in this section applies to a major transaction entered into by a receiver appointed pursuant to an instrument creating a charge over property of a company.

47 Unanimous shareholder approval - (1) Where all the shareholders of a company consent to or concur in any action taken by the company or a director, the taking of that action is deemed to be validly authorised by the company notwithstanding:

(a) any provision to the contrary in its Articles; or

(b) the absence of express authority to take such action in its Articles.

(2) The matters which may be authorised in accordance with subsection (1) include but are not limited to the following:

(a) the issue of shares;

(b) the making of a distribution;

(c) the repurchase of shares;

(d) giving financial assistance for the purpose of, or in connection with, the purchase of shares in the company;

(e) the payment of remuneration to a director, or the making of a loan to a director, or the conferral of any other benefit on a director;

(f) the making of a contract between the company and a director, or of any other contract in which a director has an interest;

(g) entry into a major transaction;

(h) the ratification after the event of any action which could have been authorised under this section.

(3) A company must not authorise a distribution under this section unless there are reasonable grounds for believing that, after that distribution is made, the company will satisfy the solvency test in section 4.

(4) Section 23 applies to a distribution made in breach of subsection (3) as if:

(a) the distribution had been made in breach of section 22; and

(b) the distribution was authorised by all shareholders.

48. Shareholder written resolutions - (1) Subject to subsection (3), a resolution in writing signed by shareholders who together hold not less than 75% of the votes entitled to be cast on that resolution at a meeting of shareholders, is as valid as if it had been passed at a meeting of those shareholders.

(2) A resolution in writing that:

(a) relates to a matter that is required by this Act or by the Articles to be decided at a meeting of the shareholders of a company; and

(b) is signed by the shareholders referred to in subsection (1) -

is made in accordance with this Act or the Articles of the company, as the case may be.

(3) If, in respect of any matter, the Articles of a company:

(a) require approval by a higher majority than 75% of those shareholders entitled to vote and voting, the reference in subsection (1) to 75% is taken to be a reference to that higher majority;

(b) specify additional requirements for approval of such matters, those requirements must also be satisfied in order for the resolution to be valid.

(4) Within 5 working days of a resolution being passed under this section, the company must send a copy of the resolution to every shareholder who did not sign the resolution.

(5) A resolution may be signed under subsection (1) or subsection (2) of this section without any prior notice being given to shareholders.

(6) If a company fails to comply with subsection (4):

(a) the company commits an offence and is liable on conviction to the penalty set out in section 194(1):

(b) every director of the company commits an offence and is liable on conviction to the penalty set out in section 195(1).

49. Shareholder meetings - (1) Meetings of the shareholders of a company must be held in accordance with the Articles**.**

(2) A special meeting of shareholders entitled to vote on an issue:

(a) may be called at any time by a director;

(b) must be called by the directors on the written request of shareholders holding shares carrying together not less than 5 per cent of the votes which may be cast on the issue.

(3) The Articles govern the procedure at meetings of shareholders.

Alteration of shareholder rights

50 Alteration of shareholder rights - (1) A company must not take action that affects the rights attached to shares unless that action has been approved by:

(a) a special resolution of each interest group; or

(b) all shareholders under section 47.

(2) For the purposes of subsection (1), the rights attached to a share include:

(a) the rights, privileges, limitations, and conditions attached to the share by this Act or the Articles, including voting rights and rights to distributions:

(b) the right to have any provisions of the Articles in relation to the issue of further shares observed by the company:

(c) the right to have the procedure set out in this section, and any further procedure required by the Articles for the amendment or alteration of rights, observed by the company:

(d) the right that a procedure required by the Articles for the amendment or alteration of rights not be amended or altered.

(3) In this section:

"Class" means a class of shares having attached to them identical rights, privileges, limitations, and conditions:

"Interest group", in relation to any action or proposal affecting rights attached to shares, means a group of shareholders:

(a) whose affected rights are identical; and

(b) whose rights are affected by the action or proposal in the same way; and

(c) subject to subsection (4)(b), who comprise the holders of one or more classes of shares in the company.

(4) For the purposes of this section and the definition of the term "interest group":-

(a) one or more interest groups may exist in relation to any action or proposal; and

(b) if:-

(i) action is taken in relation to some holders of shares in a class and not others; or

(ii) a proposal expressly distinguishes between some holders of shares in a class and other holders of shares of that class,—

holders of shares in the same class may fall into 2 or more interest groups.

Minority buy-out rights

51. Repurchase of dissenter's shares - (1) Where:

(a) a shareholder is entitled to vote on the exercise of one or more of the powers set out in:-

(i) section 44(b), and the proposed alteration imposes or removes a restriction on the activities of the company; or

(ii) section 44(c) or section 44(d); and

(b) the shareholders resolve to exercise the power; and

(c) the shareholder cast all the votes attached to shares registered in the shareholder's name and having the same beneficial owner against the exercise of the power,

that shareholder is entitled to require the company to purchase those shares in accordance with the procedure set out in the Fourth Schedule.

(2) Where:

(a) an interest group has, under section 50, approved, by special resolution, the taking of action that affects the rights attached to shares; and

(b) the company becomes entitled to take the action; and

(c) a shareholder who was a member of the interest group cast all the votes attached to the shares registered in that shareholder's name and having the same beneficial owner against approving the action,

that shareholder is entitled to require the company to purchase those shares in accordance with the procedure set out in the Fourth Schedule.

(3) Where a resolution of shareholders or of an interest group is made in writing in accordance with section 48, subsections (1) and (2) apply as if references to a shareholder who cast all the votes attached to shares registered in the shareholder's name and having the same beneficial owner against the matter in question were references to a shareholder who did not sign the written resolution in respect of such shares.

Disclosure to shareholders

52. Annual report to shareholders - (1) Subject to subsection (2), the directors of every company must, within 20 working days after the date on which the company is required to complete its financial statements under section 111:

(a) prepare an annual report on the affairs of the company during the accounting period ending on that date; and

(b) send a copy of that report to each shareholder.

(2) The Articles of a private company may provide that the directors are only required to prepare an annual report in respect of an accounting period if a shareholder has given written notice to the company prior to the end of that accounting period requiring such a report to be prepared.

(3) Every annual report for a company must –

(a) be in writing and be dated; and

(b) include financial statements for the accounting period which comply with section 111; and

(c) where an auditor's report is required under section 112 in relation to the financial statements included in the report, include that auditor's report; and

(d) state the names of the persons holding office as directors of the company as at the end of the accounting period and the names of any persons who ceased to hold office as directors of the company during the accounting period; and

(e) contain such other information as may be required by –

(i) regulations made under this Act; and

(ii) the Articles; and

(f) be signed on behalf of the directors by 2 directors of the company or, if the company has only one director, by that director.

(4) If the directors of a company fail to comply with subsection (1), every director of the company commits an offence and is liable on conviction to the penalty set out in section 195(2).

53. Inspection of company records by shareholders - A shareholder is entitled to inspect company records in accordance with section 100.

54 Other information for shareholders - (1) A shareholder may at any time make a written request to a company for information held by the company.

(2) The request must specify the information sought in sufficient detail to enable it to be identified.

(3) Within 10 working days of receiving a request under subsection (1), the company must either—

(a) provide the information; or

(b) agree to provide the information within a specified period; or

(c) agree to provide the information within a specified period if the shareholder pays a reasonable charge to the company (which must be specified and explained) to meet the cost of providing the information; or

(d) refuse to provide the information, specifying the reasons for the refusal.

(4) Without limiting the reasons for which a company may refuse to provide information under this section, a company may refuse to provide information if—

(a) the disclosure of the information would be likely to prejudice the commercial position of the company; or

(b) the disclosure of the information would be likely to prejudice the commercial position of any other person, whether or not that person supplied the information to the company; or

(c) the request for the information is frivolous or vexatious.

(5) If the company requires the shareholder to pay a charge for the information, the shareholder may withdraw the request, and is deemed to have done so unless, within 10 working days of receiving notification of the charge, the shareholder informs the company:-

(a) that the shareholder will pay the charge; or

(b) that the shareholder considers the charge to be unreasonable.

(6) The Court may, on the application of a person who has made a request for information, if it is satisfied that:-

(a) the period specified for providing the information is unreasonable; or

(b) the charge set by the company is unreasonable:-

as the case may be, make an order requiring the company to supply the information within such time or on payment of such charge as the Court thinks fit.

(7) The Court may, on the application of a person who has made a request for information, if it is satisfied that:-

(a) the company does not have sufficient reason to refuse to supply the information; or

(b) the company has sufficient reason to refuse to supply the information but that other reasons exist that outweigh the refusal:-

make an order requiring the company to supply the information.

(8) Where the Court makes an order under subsection (7), it may specify the use that may be made of the information and the persons to whom it may be disclosed.

(9) On an application for an order under this section, the Court may make such order for the payment of costs as it thinks fit.

55. Investigation at request of shareholder - (1) The Court may, on the application of a shareholder of a company, make an order authorising a person named in the order at a time specified in the order, to inspect and to make copies of, or take extracts from, the records or other documents of the company, or such of the records or documents of the company as are specified in the order, and may make such ancillary order as it thinks fit, including an order that the accounts of the company be audited by that person.

(2) The Court may make an order under subsection (1) only if it is satisfied that:

(a) in making the application, the shareholder is acting in good faith and that the inspection is proposed to be made for a proper purpose; and

(b) the person to be appointed is a proper person for the task.

(3) A person appointed by the Court under subsection (1) must diligently carry out the inspection and, having done so, must make a full report to the Court.

(4) On receiving the report of an inspector, the Court may make such order in relation to the disclosure and use that may be made of records and information obtained as it thinks fit.

(5) An order made under subsection (4) may be varied from time to time.

(6) The reasonable costs of the inspection must be met by the company unless the Court orders otherwise.

(7) A person may only disclose or make use of information or records obtained under this section in accordance with an order made under subsection (4) or subsection (5).

(8) A person who discloses or makes use of information or records obtained under this section other than in accordance with an order made under subsection (4) or subsection (5) commits an offence, and is liable on conviction to the penalty set out in section 194(2).

Minimum number of shareholders

56. Every company must have at least one shareholder - A company must at all times have at least one shareholder.

PART SIX

DIRECTORS AND THEIR POWERS AND DUTIES

57 Meaning of "director"

In this Act, "director", in relation to a company:-

(a) includes a person occupying the position of director of the company, by whatever name called; but

(b) does not include a receiver.

58. Management of company - Except to the extent that this Act or the company's Articles provide otherwise **:**

(a) the business and affairs of a company must be managed by, or under the direction or supervision of, the directors of the company.

(b) the directors of a company have all the powers necessary for managing, and for directing and supervising the management of, the business and affairs of the company.

Directors' duties

59. Fundamental duties of directors - Every director of a company must, when exercising powers or performing duties as a director, act:

(a) in good faith; and

(b) in a manner that the director believes to be in the interests of the company.

60. Duty of directors to comply with Act - A director of a company must not act or agree to the company acting in a manner that contravenes this Act.

61. Duty of directors to comply with Articles - A director of a company must not act or agree to the company acting in a manner that contravenes the company's Articles.

62. Interest of director in company transactions - (1) A director must not exercise any power as a director in circumstances where that director is directly or indirectly materially interested in the exercise of that power unless:

(a) this Act expressly authorises the director to exercise the relevant power notwithstanding such an interest; or

(b) the director has reasonable grounds for believing that the company will satisfy the solvency test after that power is exercised, and either:

(i) the Articles expressly authorise the director to exercise the relevant power notwithstanding such an interest, following disclosure of the interest in accordance with subsection (2); or

(ii) the exercise of the power by the director has been approved by all shareholders under section 47, following disclosure of the nature and extent of the director's interest to all shareholders who are not otherwise aware of those matters.

(2) A director who is directly or indirectly materially interested in the exercise of any power may only be authorised by the Articles to exercise that power if the Articles require that, prior to the exercise of the power, the director must disclose the nature and extent of that interest in writing –

(a) if there is at least one other director who is not directly or indirectly materially interested in the transaction or proposed transaction, to the directors of the company;

(b) if paragraph (a) does not apply, to all shareholders other than the director.

63. Use and disclosure of company information - A director of a company who has information in his or her capacity as a director or employee of the company, being information that would not otherwise be available to him or her, must not disclose that information to any person, or make use of or act on the information, except:

(a) in the interests of the company; or

(b) as required by law; or

(c) where there are reasonable grounds for believing that the company will satisfy the solvency test after the director takes that action, and that action:

(i) is authorised by the Articles; or

(ii) is approved by shareholders under section 47.

64. Standard of care of directors - Subject to the company's Articles, a director of a company, when exercising powers or performing duties as a director, must exercise the care, diligence, and skill that a reasonable person would exercise in the same circumstances taking into account, but without limitation:

(a) the nature of the company; and

(b) the nature of the decision; and

(c) the position of the director and the nature of the responsibilities undertaken by him or her.

65. Obligations of directors in connection with insolvency - (1) A director of a company who:

(a) believes that the company is unable to pay its debts as they fall due in the normal course of business; or

(b) is aware of matters which would put any reasonable person on inquiry as to whether the company is unable to pay its debts as they fall due in the normal course of business:-

must call a meeting of directors within 10 working days to consider whether the directors should appoint an administrator or liquidator.

(2) At a meeting called under this section the directors must consider whether to appoint an administrator or liquidator, or to continue to carry on the business of the company.

(3) If:

(a) a director fails to comply with subsection (1); and

(b) at the time of that failure the company was unable to pay its debts as they fell due in the normal course of business; and

(c) the company is subsequently placed in liquidation,

that director is liable to any creditor to whom the company incurred an obligation after that time in accordance with subsection (5).

(4) If:

(a) at a meeting called under this section the directors do not resolve to appoint an administrator or liquidator; and

(b) at the time of that meeting there were no reasonable grounds for believing that the company was able to pay its debts as they fell due; and

(c) the company is subsequently placed in liquidation,

each director other than those directors who participated in the meeting and voted in favour of appointing an administrator or a liquidator is liable to any creditor to whom the company incurred an obligation after the date of the meeting in accordance with subsection (5).

(5) A director who is liable to a creditor under subsection (3) or subsection (4) in respect of an obligation of the company is liable to that creditor for the amount of any loss suffered by that creditor as a consequence of the company's failure to perform that obligation, unless the director establishes that the creditor –

(a) knew or ought to have known of the circumstances which called into question the solvency of the company; or

(b) otherwise assumed the risk of dealing with the company in those circumstances.

(6) Where more than one director is liable to a creditor under this section, the liability of those directors is joint and several.

66. Effect of unanimous shareholder approval on certain duties of directors - If a director exercises any power or takes any other action in his or her capacity as a director with the consent or concurrence of shareholders under section 47:

(a) the director is deemed to be acting in accordance with the requirements of section 61; and

(b) if at the time the director so acts, there are reasonable grounds for believing that the company is able to meet its debts as they fall due, that director is deemed to be acting in accordance with the requirements of sections 59 and 64.